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Workers' Compensation: Frequently Asked Questions

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Workers' compensation programs were originally set up to provide prompt medical treatment and lost time benefits to injured workers in exchange for certain legal protections for the employer. Generally, workers' compensation is considered the exclusive remedy for workplace injuries and illnesses.

The State has experienced increases in workers' compensation expenses resulting from the aggressive closure of open cases during FY 2002. The State's professional third party administrator (TPA), Sedgwick Claims Management Services (SCMS), has effectively reduced the State's future liabilities by closing 80 percent of open cases as of March, 2002; and continues to assist IDOP in gaining greater control over program expenses.

1. **How does the workers' compensation program work?** Today, workers' compensation is a State-mandated benefit under Chapters 85, 85A and 85B of the Iowa Code for *all* 60,000+ State employees. Benefits may include payment of wage replacement benefits beginning the fourth day off work (excluding the day of injury) and payment of medical bills. State employees can elect to supplement their temporary disability benefits with sick leave, vacation, or compensatory time.

2. **How does an employee use the program?** An employee who has suffered an injury begins the process by notifying a supervisor. The supervisor sees that a First Report of Injury (FROI) is completed by either assisting the employee or involving the agency's workers' compensation coordinator. The agency forwards a completed FROI to SCMS. The program refers the employee to a health care provider for medical care and initiates lost time benefits if appropriate.

3. **Who administers the program for State employees?** The Iowa Department of Personnel (IDOP) has statutory authority and overall program management responsibility for administering the workers' compensation program for State employees under Section 19A.32 of the Iowa Code.

   IDOP sees that the program meets regulatory requirements, assesses the employing departments for premiums to fund the program, and provides loss information and loss control services to the agencies. Program support staff includes a bureau chief, one accountant, one safety officer and one return to work coordinator. Legal assistance is provided by the Office of the Attorney General when litigation takes place.

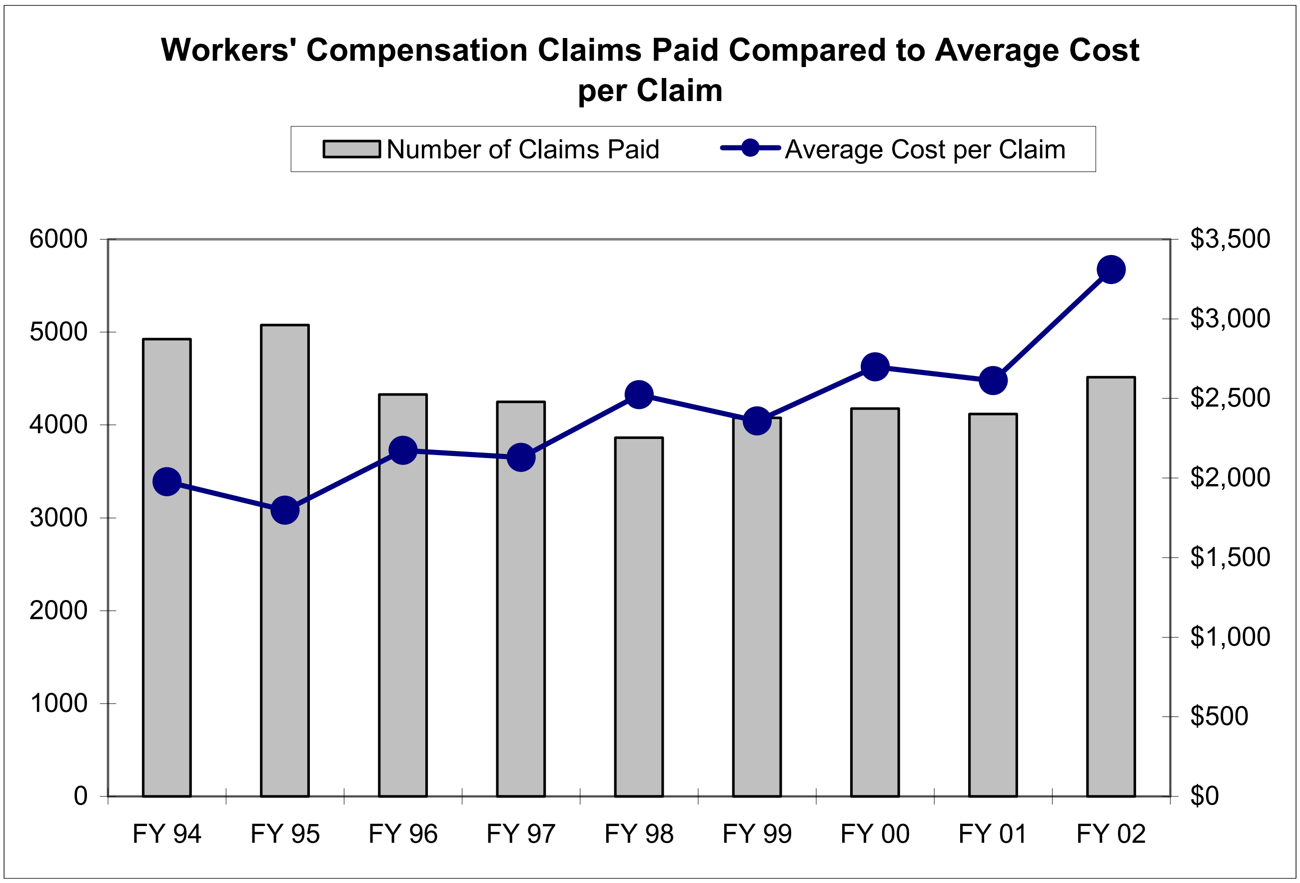
   Agencies have a critical role in managing losses caused by work-related injury and illness. IDOP provides ongoing education and consultation, both directly and through SCMS, to assist agencies with this role.

   Beginning in FY 2002, IDOP retained SCMS to handle day-to-day claims management. This decision was made in response to recommendations from the State's benefits consultant, the Segal Company, in order to improve program performance from a financial and compliance perspectives.

4. **How is the program funded?** The State of Iowa's program is self-funded. To cover the costs,

IDOP determines a premium charge that is based on the loss history of each agency and the program's unpaid liabilities. For FY 2003, administrative fees (primarily the cost of the TPA) are allocated to each agency as a percent of estimated payroll. IDOP notifies each agency regarding the fee amount and bills agencies for the premiums in quarterly increments.

5. **What has happened to workers' compensation costs during recent years?** The chart below illustrates the number of claims and average cost per claim from FY 1994 to FY 2002, the most recent period for which data is available. Total claims expenses (excluding administrative costs) were generally stable from 1994 through 1999, at an annual average outlay of $9.42 million. Claims costs rose to $11.26 in FY 2000, $10.76 million in 2001, and $14.94 million in FY 2002. (Administrative costs for FY 2002 were $2.05 million.)



6. **Why the increase in premium expense?** In FY 2002, IDOP collected $12.9 million in premium payments from agencies. More than $17 million in expenses were incurred during that period, due to accelerated claims payments and increased administrative costs. The difference between premiums and expenses was paid from workers' compensation fund surpluses.

   In FY 2003, IDOP is billing agencies a total of $17.39 million, a 35 percent increase. This increase reflects IDOP's continued efforts to settle a greater number of claims than in past years, an action that reduces future program liability. The distribution of this cost increase varies by agency. Some 42 agencies saw no increase. Three agencies saw increases of more than $100,000.

7. **How were the premium increases calculated?** IDOP reviewed paid loss data for each agency from 1996 to present, added in SCMS's estimate for the amount required for future reserves and calculated the average loss per agency. This became the base premium.

8. **What factors are driving program costs?** Two primary factors affect costs for this program. First, the cost of medical care rises when providers raise their rates or when utilization of providers increases. Second, increases in employee wages cause increases in program costs because the program replaces employee wages following an injury when the employee is eligible for that benefit.

   SCMS assists the State in controlling all program expenses through more aggressive claims settlement and case management. The cost of the TPA is built into premium expenses beginning in FY 2003.

9. **What is the total administrative expense for the program?** The total administrative costs charged to agencies for this program are about $3 million in FY 2003. The non-TPA program expenses include costs of banking, internal data processing, and other administrative expenses. Direct General Fund appropriations offset internal IDOP administrative costs and the cost of legal support provided by the Office of the Attorney General.

10. **What happens if the State does not fully fund workers' compensation expenses?** Full funding of this program would include money to pay current claims and administrative expenses and funds set aside to cover future unpaid liabilities. If funding is less than the amount needed to pay all current claims, claims payments will be pushed to the future where they will generally cost more.

    Paying claims more slowly leaves the State open to several risks. First, the chance of litigation increases, and data shows that the cost of litigated claims is higher than non-litigated claims. Second, cost shifting to the future increases the program's unpaid liability. Both of these factors mean greater long-term future cash outlay or liability at comparatively higher costs.

    It is important to note that the amount of money currently collected for workers' compensation expenses barely funds current claims and administrative costs. NO funds are being set aside to manage cash flow crunches, catastrophic claims costs, or future unpaid liabilities.

11. **What is the longer-term outlook for program costs?** Involving a TPA to more aggressively manage and close claims will ultimately reduce the unpaid liability of this program. Over the short term, however, the transition has resulted in an anticipated cost spike of uncertain duration. The spike is the result of changes in claims handling practices, inflation, and the cost of new claims entering the system more rapidly than under the previous methodology. Effective claims management and resolution by SCMS coupled with more effective control of new losses will reverse the spike.

    A comprehensive evaluation of longer-term program costs requires an updated actuarial review to assess liabilities. IDOP is now initiating such a review, which will also include recommendations regarding fair allocation of program costs to customer agencies.

12. **What results has SCMS achieved to date?** By contract, key SCMS activities are monitored to allow evaluation of performance. These measures include closed file ratios, review and update of diaries, new claims set up, medical bill processing, reserve updating, supervisor review audits, and timely initial contact. At the end of contract year 1, SCMS performance exceeded corporate targets for all measures.

    In the closed file ratio category, SCMS has enabled the closure of nearly 80 percent of the previously opened, newly opened or reopened cases since the State's contract began (July, 2001 through March, 2002.) Some $8.5 million was expended in FY 2002 to eliminate additional liability on FY 2001 or older claims from the State's incurred but unpaid liability. Some 20 percent of litigated files were resolved and more than $1.5 million was spent closing new FY 2002 claims.

    Reduction of the average cost per new claim by 10 percent is also a program goal, and this goal was not met. In fact, although contracting with SCMS has substantially decreased the number of unnecessary medical visits, decreasing utilization, the cost of medical care provided to employees under the program has increased. Discussions with the current network to remedy this situation are underway.

13. **What can State agencies do to help improve performance and reduce our premiums?** Two general factors affect claims: frequency and severity. Frequency is the number of claims filed; employers who reduce frequency avoid the cost of some claims altogether. Severity refers to the seriousness of the claim; reductions in severity reduce the final cost of the claim.

    Data proves that, when there is a culture of safety in an organization and compliance is encouraged, costs go down. Safety programs can reduce both frequency and severity. An effective return to work program will reduce the severity of claims, because employees who do not return to work after an on-the-job injury may be entitled to additional workers' compensation and other State sponsored benefits like long-term disability.

    Some elements of successful efforts to reduce or control workers' compensation claims include:

    - A strong management commitment to program compliance;
    - Hazard analysis to maximize safety in the workplace;
    - Ongoing program evaluation and improvement;
    - An early return to work policy to maximize employee productivity.

    Inflation will always be a problem. Constant monitoring will assure that high quality, effective services are applied to address the State's workers' compensation program.